

## California Divests Iranian Investors

**Publication Date: May 02, 2011**

During summer 2010, many of the developed nations initiated sanctions against Iran, a signal that their political discourse was supported by economic realities. In the United States, that movement culminated in the Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010 ("CISADA"), which was signed into law July 1, 2010. While a great deal of attention was given to the sanctions related to petroleum investment and financial intuitions, one element of the law was left in the relative background, until now.

Section 202 of CISADA granted state and local governments the authority to divest the assets of the state or local government from persons who were engaged in investment activity in Iran. In passing the Iran Contracting Act of 2010 ("ICA"), California has chosen to exercise the authorization granted by the CISADA.

### Prohibitions

The goal of the ICA, as was the goal of CISADA, is to force individuals and entities who wish to do business with the government of California, and local California bodies, to cease investment in Iran. The ICA achieves its goal by requiring the Department of General Services ("DGS") to establish a list of persons and entities that engage in investment activities in Iran. The prohibited investments fall into two categories:

- An investment of goods or services of \$20 million or more in the energy sector of Iran
- A financial institution's extension of credit for 45 days of at least \$20 million if that extension of credit is to be used in the energy sector in Iran

The resulting list created by the Department of General Services essentially becomes the "Black List" of California government contractors. Absent an exception, entities on the Black List are prohibited from bidding on, or renewing, a contract with the state of California, or local California bodies, for goods or services in excess of \$1 million.

## **Black List**

The California Department of General Services is required to initiate the formation of the list by June 1, 2011. As a result, persons who invest in Iran, have invested in Iran, or have been perceived as having invested in Iran, are encouraged to be vigilant regarding potential notice from the DGS. The only criterion the DGS needs in order to place a person on the Black List is "credible information available to the public."

While placement on the Black List would prohibit contracting with California, the ICA does provide industry with a vehicle to fight such a listing. Prior to DGS making a final determination as to a specific person's placement on the list, that person is required to receive written notice 90 days in advance. That notice will provide the person with the opportunity to comment in writing, refuting the claim that the person is engaged in Iranian investment activities, as defined.

Once an individual or entity has received notice of the DGS's intention to place them on the Black List, that person must act quickly in order to avoid being banned from contracting with California. By refuting a claim of Iranian investment to the satisfaction of the DGS, that person shall not be placed on the Black List and will remain eligible to contract with California. Failure to refute a claim by DGS will result in a person being placed on the Black List and will likely result in significant interruptions to business operations.

## **Exceptions**

The ICA does provide two exceptions, through which persons that invest in Iran will not be prohibited from contracting with California. The first exception requires a finding that, despite the Iranian investment, the contract with the person is in the best interest of the state or local public entity; the investment in Iran was made before July 1, 2010; the investment has not expanded since July 1, 2010; and the person is implementing a plan to cease investment in Iran and refrain from any new investment.

The second exception requires either the state or local entity to make a determination that without the contract, it would not be able to obtain the goods or service that person provides.

## **Obligations and Penalties**

Under the ICA, potential contractors have an affirmative obligation when bidding or renewing contracts in excess of \$1 million. The obligation is to certify that they are not currently listed on the Black List, nor are they engaged in investment activities in Iran (having merely avoided detection and placement on the Black List).

If a person submits a false certification regarding their investment in Iran, they are subject to several penalties:

- Civil penalty in the amount of \$250,000 or twice the amount of the contract
- Termination of the contract
- Three-year ban on contracting with California

## **Conclusion**

If you receive notice from the California Department of General Services that your business is to be listed as engaging in prohibited investment in Iran, you have a limited window to refute this claim. It is imperative to act quickly so as to avoid an interruption in your business operations and to curtail any negative implications. Please contact Leigh Hansson, Michael Lowell, Michael Grant, or your regular Reed Smith attorney for more advice on this or other export matters.